

AGENDA

ASSEMBLY BUDGET COMMITTEE SECOND EXTRAORDINARY SESSION

ASSEMBLYMEMBER NANCY SKINNER, CHAIR

WEDNESDAY, MAY 14, 2014

2:00 PM - STATE CAPITOL ROOM 447

PART 1

<u>FILE ORDER</u>	<u>BILL</u>	<u>AUTHOR</u>	<u>SUBJECT</u>	<u>PAGE</u>
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Date of Hearing: May 14, 2014

ASSEMBLY COMMITTEE ON BUDGET X2

Nancy Skinner, Chair

ACA 1 X2 (John A. Pérez) – As Amended: May 12, 2014

SUBJECT: State Budget Reserve

SUMMARY: Makes changes to the State's budget reserve policy. Specifically, this measure:

- 1) Removes Assembly Constitutional Amendment 4 (Gatto), Resolution Chapter 174 of the Statutes of 2010, from the 2014 General Election ballot.
- 2) Doubles the size of the Budget Stabilization Account (BSA) from five percent of the General Fund (or \$8 billion, whichever is greater) to 10 percent of the General Fund.
- 3) Eliminates the current three percent of General Fund revenues contribution to the BSA.
- 4) For fiscal years 2015-16 through 2029-30, requires half of the amounts listed below to be deposited into the BSA and the other half to be appropriated for specified debt obligations. Beginning in 2030-31 up to 50 percent of the amounts may be used for specified debt obligations, with the balance deposited into the BSA.
 - a. 1.5 percent of General Fund revenues.
 - b. Revenues not required for Prop 98 that are derived from taxes on Capital Gains that make up more than eight percent of total General Fund revenues. Calculations regarding capital gains calculations will be “trued-up” over the following two fiscal years.
 - c. Specifies that the transfer of revenue to the BSA would take place on October 1st.
 - d. Defines eligible debt obligations as current Proposition 98 settle up, existing General Fund loans that had balances on January 1, 2014, prior year mandated costs, and unfunded retirement liabilities.
- 5) Limits suspensions of transfers into the BSA and withdrawals from the BSA to the following circumstances:
 - a. A disaster, as currently defined in Article XII B of the State Constitution.

- b. Insufficient revenues to fund the budget at the level of the highest previous three years, adjusted for populations and inflation. The suspension/withdrawal is limited to the amount needed to reach that level.
 - c. Restricts the amount of funding that can be transferred from the Budget Stabilization Account to the General Fund to 50 percent of the BSA's balance, unless a transfer was made in the prior year.
- 6) Once the BSA reaches 10 percent, restricts the use of any funds that otherwise would be deposited into the BSA infrastructure appropriations, including deferred maintenance.
- 7) Creates a Proposition 98 Reserve, called the Public School System Stabilization Account, which would capture certain revenues derived from taxes Capital Gains and attributed to Proposition 98 purposes in very specific circumstances:
 - a. The State must have repaid and allocated the entire Proposition 98 Maintenance Factor amount before a transfer could be made.
 - b. The State must be in a Test 1 level of Proposition 98 and the transfer can be no more than the difference between the Test 1 and Test 2 levels of Proposition 98.
 - c. The State cannot be accruing Proposition 98 Maintenance Factor or have suspended Proposition 98 in a year when the transfer is made.
 - d. If these conditions are met, Proposition 98's share of revenues derived from capital gains that are above 8percent of total General Fund are transferred into the Proposition 98 reserve.
 - e. These funds would be used to fund Proposition 98 Growth and Cost of Living Adjustments in years when there is a decline in Proposition 98.
 - f. Transferred funds would be considered part of the Proposition 98 calculation.
- 8) Requires the Department of Finance to submit five-year General Fund revenue and expenditure projections as part the budget submission. This places a current statutory requirement into the State Constitution.
- 9) Requires the display of the calculations for this measure and the overall balance of the Budget Stabilization Account in the Budget Act.

EXISTING LAW Article XVI of the State Constitution includes language related to Proposition 58 which established the Budget Stabilization Act and includes an optional transfer of 3 percent of overall General Fund revenues, which can be suspended by the Governor. This language caps the size of the Budget Stabilization Account at five percent of the General Fund (or \$8 billion, whichever is greater).

FISCAL EFFECT: Compared with current Constitutional requirements, this measure will result in bigger BSA contributions and debt payment obligations during “boom” years and smaller contributions during ordinary years. In the 2014-15 May Revision, the Department of Finance provided the following estimates of the transfers and debt repayments for the first three fiscal years that this new measure would be in effect:

Calculation of Rainy Day Amounts at 2014-15 May Revision			
	2015-16	2016-17	2017-18
Annual 1.5 percent General Fund Revenue Transfer	\$ 1,698	\$ 1,773	\$ 1,854
Capital Gains Tax Revenue above 8 percent of Total General Fund Revenues	\$ 174	\$ 233	\$ 341
Total Rainy Day Fund Amount	\$ 1,872	\$ 2,005	\$ 2,195

Debt Repayment	\$ 936	\$ 1,003	\$ 1,097
Deposit to Budget Stabilization Account	\$ 936	\$ 1,003	\$ 1,097

COMMENTS: Assembly Constitutional Amendment 1 X2 responds to two critical problems that have plagued California’s budget for decades:

1. **Revenue Volatility.** California’s revenue system is notoriously volatile. This results in large part from reliance on income tax. While income tax rates are not dramatically progressive, the incomes of wealthy Californians do fluctuate and therefore their income taxes they pay also fluctuate.
2. **Inadequate Reserves.** Long term forecasts are always difficult. At times forecasts show balanced budgets as far as the eye can see, but reality often proves different. Without strong reserves, unpredicted economic down turns have ravished the state budget and caused draconian cuts to programs and painful middle class tax increases.

ACA 1 X2 addresses these problems with the following:

1. **Stabilizes Spending.** ACA 1 X2 separates state spending from the rollercoaster of revenue volatility. This measure takes capital gains revenues that make up more than eight percent of the General Fund – the average for the last 10 years – off the table rather than being used for unsustainable permanent tax cuts or ongoing programs. The spiking revenues (along with 1.5 percent of overall General Fund revenues) will be used for debt payments and deposited into the BSA, to be withdrawn during economic downturns to avoid program cuts and middle class tax increases.
2. **Increases the Reserve.** ACA 1 X2 doubles the size of the Constitutional Reserve to 10 percent, which will provide increased protection against draconian cuts to programs and painful middle class tax increases during economic down turns.

REGISTERED SUPPORT / OPPOSITION:

Support

Governor Jerry Brown

Kern County Superintendent of Schools

California Forward

Opposition

Riverside County Superintendent of Schools

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